

Office of Chief Counsel
Internal Revenue Service
memorandum

CC: LM: RFP: CHI: 2: POSTF-137259-02
CAGruber

date: *August 14, 2002*

to: [REDACTED], Revenue Agent, LMSB Group [REDACTED]

from: Associate Area Counsel (LMSB), Chicago

subject: [REDACTED]
Requests for [REDACTED], [REDACTED] and [REDACTED] refunds

This memorandum responds to your request for assistance. It should not be cited as precedent. The issue does not appear to be within the responsibility of any industry counsel.

Issue: Whether the taxpayer made a timely claim for a refund of taxes paid in connection with disallowed airline expenses attributable to corporate-owned aircraft during the taxable years [REDACTED]; [REDACTED] and [REDACTED]. Additionally, assuming the taxpayer made a timely claim for a refund, should the Service grant the request for said taxes paid.

Facts: [REDACTED]
(hereinafter the "taxpayer") filed federal income tax returns for the years ending December 31, [REDACTED]; December 31, [REDACTED] and December 31, [REDACTED] which were examined as part of a CEP examination. Various expenses relating to employees' use of corporate aircrafts were disallowed in each of the tax years as part of the examination. On [REDACTED], a signed Form 870, Waiver of Restrictions on Assessment and Collection of Deficiency and Tax and Acceptance of Overassessment, was received by the Service.¹ On [REDACTED]², taxpayer also paid the net deficiency due for the three years under examination of \$[REDACTED], which was computed as follows:

¹During the [REDACTED] - [REDACTED] examination cycle, the taxpayer extended the statute of limitations of the December 31, [REDACTED], [REDACTED] and [REDACTED] tax years until [REDACTED].

²It is not known when the taxpayer paid the tax per the Services' transcript. Presumably, it would be a few weeks following [REDACTED].

December 31, [REDACTED]	(\$ [REDACTED])
December 31, [REDACTED]	\$ [REDACTED]
December 31, [REDACTED]	(\$ [REDACTED])

Total Deficiency	\$ [REDACTED]

On March 28, 2000, Sutherland Lumber-Southwest, Inc. v. Commissioner, 114 T.C. 197 (2000), was decided against the government.³ As a result, on [REDACTED], the taxpayer provided, to the audit team, a disclosure statement pursuant to Rev. Proc. 94-69 for the [REDACTED]-[REDACTED] examination cycle. The taxpayer claimed that airline expenses for the years [REDACTED]; [REDACTED] and [REDACTED] were properly deducted. On [REDACTED], the taxpayer filed Amended U.S. Corporation Income Tax Returns for the taxable years [REDACTED]; [REDACTED] and [REDACTED], seeking refunds in the amounts of \$[REDACTED]; \$[REDACTED] and \$[REDACTED], respectively. The Cincinnati, Ohio Service Center denied the claims as untimely on [REDACTED].

Analysis: A claim for credit or refund of an overpayment of any tax imposed by this title in respect of which tax the taxpayer is required to file a return shall be filed by the taxpayer within 3 years from the time the return was filed or 2 years from the time the tax was paid, whichever of such period expires the later, or if no return was filed by the taxpayer, within 2 years from the time the tax was paid. I.R.C. § 6511(a).

Because the time for assessments with respect to the [REDACTED]-[REDACTED] years was extended to [REDACTED] by agreement between the taxpayer and the Service, the time for filing a refund claim under I.R.C. § 6511(a) was extended by § 6511(c)(1) to within six months of that date, or [REDACTED]. However, a refund claim filed after the statutory limit established by § 6511(c)(1) is still considered timely under § 6511(a), for amounts paid within two years of the claim. See §§ 6511(c)(3)(B) and 6511(a).

³ The Service ultimately acquiesced in the decision of the Eighth Circuit upholding the decision of the Tax Court on February 1, 2002, stating the "Service would no longer litigate the I.R.C. § 274(e)(2) issue in cases where the taxpayer demonstrates that it has properly included in compensation and wages the value of an employee vacation flight in accordance with Treas. Reg. § 1.61-21(g). In those cases the Service will allow the taxpayer a full deduction for the cost of the flight. However, the Service will continue to apply § 274(a) to cases in which the value of an employee vacation flight is not included in compensation and wages." See AOD dated February 11, 2002.

The taxpayer's refund claim was not filed within six months after the expiration date of the extension agreement { [REDACTED] }. Consequently, the provisions of § 6511(c) do not affect the outcome herein.⁴

If the taxpayer made "payments" toward deficiencies for each of the [REDACTED]-[REDACTED] years after [REDACTED], the claims, for said amounts, filed on [REDACTED], would be timely. However, it is our understanding the taxpayer made only one payment on or after [REDACTED]. This should be verified through the transcripts.

Assuming the taxpayer made one "payment"⁵, toward the [REDACTED] deficiency, after [REDACTED], the issue to be resolved is whether the claim should be allowed. As set forth in the Form 886-A, Explanation of Items relative to the airline adjustment for years [REDACTED], "[f]or a deduction to be allowed for any item under § 274(a)(1)(A), the taxpayer must establish that the item was directly related to the active conduct of the taxpayer's trade or business or, in the case of an item directly preceding or following a substantial and bona fide business discussion, that such item was associated with the active conduct of the taxpayer's trade or business. . . To date [the taxpayer] has failed to show that trips were 'directly related' to the active

⁴The disclosure statement received by the audit team on [REDACTED], does not constitute an informal claim for the taxable years [REDACTED]-[REDACTED]. A valid informal refund claim requires a showing that the Commissioner was on either actual or constructive notice that a right was being asserted with respect to an overpayment of tax for a **certain year** and that there exists some sort of written component, whether created by the taxpayer or the Service. VDO-ARGO Instruments, Inc. v. United States, 83-2 U.S.T.C. (CCH) ¶9605 (Cl. Ct. 1983), aff'd without opinion, 738 F.2d 453 (Fed. Cir. 1984). The disclosure statement does **not** in any way assert a claim for airline expenses for [REDACTED]-[REDACTED].

⁵The amount of refund to which the taxpayer is entitled is limited by § 6511(b)(2) to the portion of the tax that it paid within two years preceding [REDACTED], namely, to the amounts of the deficiencies that it paid in cash, or by application of credits from other years after [REDACTED]. Given the taxpayer paid a "net deficiency" for the three years, it does not appear that a "payment" was made towards [REDACTED] and [REDACTED] within two years of [REDACTED]. See Republic Petroleum Corporation v. United States, 613 F.2d 518 (5th Cir. 1980). Consequently, the taxpayer, in all likelihood, is not entitled to any refund for the years [REDACTED] and [REDACTED].

[REDACTED]

[REDACTED] The write-up concluded that § 274(a) precludes the taxpayer from deducting the expenses it incurred in providing the [REDACTED] for employees and other family members and/or friends, except to the extent the taxpayer treated such expenses as income to employees.

For taxable year [REDACTED], the taxpayer claimed airline expenses, on the original return, in the amount of \$ [REDACTED], of which \$ [REDACTED], was disallowed. As a result of the amended [REDACTED] return, the taxpayer is requesting an additional airline expense deduction in the amount of \$ [REDACTED].

While it is true the Service has acquiesced in the holding of Sutherland Lumber, the Service will only allow the taxpayer a full deduction for the cost of the flight, provided the taxpayer demonstrates that it has properly included in compensation and wages the value of an employee vacation flight in accordance with Treas. Reg. 1.61-21(g). For other flight benefits not included as compensation or wages, the Service will continue to apply § 274(a). [REDACTED], (b)(5)(DP), (b)(7)a [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

This writing may contain privileged information. Any unauthorized disclosure of this writing may have an adverse effect of privileges, such as the attorney-client privilege. If disclosure becomes necessary, please contact this office for our views.

Should you have any questions, I can be reached at (414) 297-4243.

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By: _____
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